

Corporate Governance Under Stress: An Analysis of Insolvency Proceedings in India

Chhaya Chaudhary¹, Dr. Neha Susan Varghese²

Amity Law School, Noida, Amity University

Abstract: *Corporate governance plays a pivotal role in ensuring transparency, accountability, and ethical conduct within corporate entities. However, situations of financial distress and insolvency often place significant strain on established governance frameworks, exposing structural weaknesses and managerial inefficiencies. This study, titled “Corporate Governance under Stress: An Analysis of Insolvency Proceedings in India,” critically examines the interplay between corporate governance mechanisms and insolvency resolution processes under the Insolvency and Bankruptcy Code, 2016 (IBC). The research explores how insolvency proceedings alter traditional governance structures by shifting control from the board of directors to insolvency professionals and creditor committees. It analyses the effectiveness of this transition in preserving the interests of stakeholders, particularly creditors, minority shareholders, and employees. The study also evaluates the role of key institutions such as the Insolvency and Bankruptcy Board of India (IBBI), National Company Law Tribunal (NCLT), and resolution professionals in maintaining governance standards during the Corporate Insolvency Resolution Process (CIRP). Further, the paper identifies recurring challenges, including delays in resolution, information asymmetry, lack of accountability among resolution applicants, and potential misuse of legal provisions. Through doctrinal and analytical methods, supported by select case studies, the research highlights how governance lapses before insolvency often exacerbate financial distress, thereby complicating the resolution process. The study also assesses whether the IBC framework adequately balances the objectives of value maximization, timely resolution, and equitable treatment of stakeholders while upholding principles of good governance. It argues that although the IBC has significantly improved creditor rights and streamlined insolvency procedures, gaps remain in ensuring transparency, ethical conduct, and long-term corporate discipline. In conclusion, the paper suggests reforms aimed at strengthening corporate governance during insolvency, including enhanced regulatory oversight, stricter compliance requirements, improved capacity of adjudicating authorities, and greater emphasis on accountability mechanisms. The findings contribute to the broader discourse on corporate governance reform in emerging economies and underscore the need for a resilient insolvency framework that can withstand periods of financial stress while safeguarding stakeholder interests.*

Keywords: Corporate Governance, Insolvency and Bankruptcy Code, Insolvency and Bankruptcy Board of India (IBBI), Resolution Professionals, Corporate Failure

1. Introduction

Corporate governance has emerged as a cornerstone of modern corporate regulation, embodying the principles of transparency, accountability, and ethical management. It defines the framework within which corporate entities operate and interact with stakeholders, including shareholders, creditors, employees, and regulators. In a rapidly evolving economic environment, particularly in emerging economies like India, the importance of sound corporate governance cannot be overstated. It not only enhances investor confidence but also ensures the long-term sustainability and financial stability of corporate entities. In India, the development of corporate governance norms has been shaped by both global influences and domestic challenges. Regulatory reforms, particularly after major corporate scandals, have sought to strengthen oversight mechanisms and ensure responsible corporate behaviour. The enactment of the Companies Act, 2013, and the introduction of stricter disclosure norms under the Securities and Exchange Board of India (SEBI) regulations reflect a growing emphasis on governance standards. However, despite these advancements, corporate failures continue to occur, raising serious concerns about the effectiveness of governance frameworks in times of financial distress¹.

Financial distress represents a critical phase in the life cycle of a corporation, where the sustainability of the business is

threatened due to an inability to meet financial obligations. During such periods, governance structures are subjected to immense pressure, often exposing underlying weaknesses such as a lack of transparency, inadequate risk management, and ineffective board oversight. It is in these moments of crisis that the resilience of corporate governance mechanisms is truly tested. Weak governance not only contributes to the onset of financial distress but also complicates the resolution process, adversely affecting stakeholder interests.

The introduction of the Insolvency and Bankruptcy Code, 2016 (IBC), marked a significant milestone in India's legal and economic landscape. Before its enactment, the insolvency framework in India was fragmented and inefficient, characterised by prolonged delays and low recovery rates. Multiple laws, such as the Sick Industrial Companies Act (SICA), the Recovery of Debts Due to Banks and Financial Institutions Act, and the Companies Act provisions, operated in isolation, leading to overlapping jurisdictions and procedural inefficiencies². The IBC sought to address these issues by providing a consolidated and time-bound mechanism for insolvency resolution, thereby improving creditor confidence and promoting ease of doing business. One of the defining features of the IBC is its “creditor-in-control” model, which marks a departure from the traditional “debtor-in-possession” approach. Under this framework, once insolvency proceedings are initiated, the management of the corporate debtor is transferred from the existing board of

¹ Ministry of Corporate Affairs, *Report on Corporate Governance in India* (2019).

² Eradi Committee Report on Bankruptcy Law Reforms (2000).

directors to an insolvency professional. The decision-making authority is vested in the Committee of Creditors (CoC), which primarily comprises financial creditors. This shift fundamentally alters the corporate governance structure, raising important questions about accountability, transparency, and stakeholder representation³.

The transformation of governance during insolvency proceedings presents a unique set of challenges. While the IBC aims to ensure efficient resolution and value maximisation, the displacement of the board and concentration of power in the hands of creditors may lead to governance gaps. For instance, operational creditors, employees, and minority shareholders often have limited participation in the decision-making process, which may result in inequitable outcomes. Furthermore, the reliance on the commercial wisdom of the CoC, with limited judicial intervention, has sparked debates regarding the adequacy of checks and balances within the system⁴.

Another critical aspect of corporate governance under stress is the role of insolvency professionals. These professionals are entrusted with managing the affairs of the corporate debtor during the resolution process. Their responsibilities include preserving the value of assets, ensuring compliance with legal requirements, and facilitating the preparation of resolution plans. However, concerns have been raised regarding their accountability, competence, and independence. Instances of mismanagement or conflict of interest can undermine the integrity of the insolvency process and erode stakeholder trust. The institutional framework established under the IBC plays a crucial role in maintaining governance standards during insolvency proceedings. The Insolvency and Bankruptcy Board of India (IBBI) acts as the regulatory authority overseeing insolvency professionals and agencies, while the National Company Law Tribunal (NCLT) serves as the adjudicating authority. Together, these institutions are responsible for ensuring that the insolvency process is conducted in a fair, transparent, and efficient manner. However, challenges such as case backlogs, infrastructural limitations, and procedural delays continue to affect the effectiveness of these institutions⁵.

Judicial interpretation has also played a significant role in shaping the contours of corporate governance under the IBC framework. The judiciary has consistently emphasized the importance of adhering to the objectives of the Code, particularly the need for timely resolution and value maximization. At the same time, courts have generally refrained from interfering in the commercial decisions of the CoC, thereby reinforcing the creditor-centric approach. While this approach enhances efficiency, it also raises concerns about the potential marginalisation of other stakeholders and the absence of adequate oversight mechanisms⁶. It is also important to recognise that insolvency is often the culmination of prolonged governance failures. Issues such as lack of board independence, inadequate internal controls, financial misreporting, and unethical business practices contribute significantly to corporate distress. In many cases,

early warning signs are either ignored or inadequately addressed, allowing problems to escalate into full-blown insolvency. Therefore, the study of corporate governance under stress must also consider the pre-insolvency phase and the role of preventive governance mechanisms.

In the Indian context, high-profile insolvency cases have highlighted both the strengths and weaknesses of the IBC framework. While the Code has facilitated faster resolution and improved recovery rates in several cases, it has also exposed challenges such as litigation delays, valuation disputes, and concerns regarding transparency. These issues underscore the need for continuous evaluation and reform of the insolvency framework to ensure that it aligns with the principles of good corporate governance.

This research paper seeks to analyse the dynamics of corporate governance during insolvency proceedings in India, with a particular focus on the stress factors that influence decision-making and stakeholder outcomes. It aims to examine whether the current framework effectively balances the objectives of efficiency, fairness, and accountability, or whether it disproportionately favours certain stakeholders. The study adopts a doctrinal and analytical approach, drawing upon statutory provisions, judicial decisions, and academic literature to provide a comprehensive understanding of the subject. The significance of this study lies in its attempt to bridge the gap between corporate governance theory and insolvency practice. While governance principles are well-established in stable corporate environments, their application during periods of financial distress remains complex and contested. By exploring the intersection of governance and insolvency, this research contributes to the broader discourse on corporate regulation and economic reform in India.

In conclusion, corporate governance under stress represents a critical area of study in contemporary legal and economic scholarship. The IBC has undoubtedly transformed the insolvency landscape in India, but its success in ensuring robust governance during distress remains subject to debate. Strengthening governance mechanisms within the insolvency framework is essential not only for achieving effective resolution but also for fostering trust and stability in the corporate sector. This paper endeavours to shed light on these issues and propose pathways for reform that can enhance the resilience and integrity of India's corporate governance regime. Corporate governance refers to the system of rules, practices, and processes by which companies are directed and controlled. It ensures accountability, fairness, and transparency in a company's relationship with its stakeholders. In India, corporate governance has gained prominence, particularly after financial scandals and corporate failures exposed weaknesses in regulatory frameworks. However, the true test of governance mechanisms arises during periods of financial distress, especially insolvency. The enactment of the Insolvency and Bankruptcy Code, 2016 (IBC) marked a transformative step in India's insolvency regime. It introduced a creditor-driven process aimed at timely resolution of stressed assets while

³ Insolvency and Bankruptcy Code, 2016, Sections 17–21.

⁴ Committee of Creditors of Essar Steel India Ltd. v. Satish Kumar Gupta.

⁵ Insolvency and Law Committee Report (2020).

⁶ Swiss Ribbons Pvt. Ltd. v. Union of India.

maximizing value. Yet, insolvency proceedings inherently disrupt traditional governance structures by transferring control from the board of directors to insolvency professionals and creditors. This shift raises critical concerns regarding governance standards, stakeholder protection, and ethical decision-making.

This paper examines how corporate governance operates under stress during insolvency proceedings, highlighting key challenges, institutional roles, and areas requiring reform.

Concept of Corporate Governance

Corporate governance encompasses principles such as transparency, accountability, responsibility, and fairness in corporate functioning. It involves various stakeholders, including shareholders, directors, creditors, employees, and regulators.

The Organisation for Economic Co-operation and Development (OECD) defines corporate governance as a system through which companies are directed and controlled, emphasizing the distribution of rights and responsibilities among stakeholders⁷.

In India, governance norms are primarily governed by:

- Companies Act, 2013
- SEBI (LODR) Regulations
- Judicial precedents

Effective governance ensures:

- Protection of shareholder rights
- Ethical corporate behavior
- Risk management and compliance

However, weak governance structures often lead to financial mismanagement and eventual insolvency.

Insolvency Framework in India

The introduction of the Insolvency and Bankruptcy Code, 2016 consolidated fragmented insolvency laws into a unified framework. The Code provides a time-bound process for resolving insolvency of corporate persons, partnership firms, and individuals.

Key features include:

- Time-bound resolution (180–330 days)
- Creditor-in-control model
- Moratorium on legal proceedings
- Establishment of institutional framework

Important institutions under IBC:

- Insolvency and Bankruptcy Board of India (IBBI)
- National Company Law Tribunal (NCLT)
- Insolvency Professionals (IPs)

The Corporate Insolvency Resolution Process (CIRP) begins when a company defaults on its debt. Control of the company is transferred from the board to an insolvency professional, fundamentally altering governance structures.

Shift in Corporate Governance during Insolvency

One of the most significant changes during insolvency is the displacement of the board of directors. The management is taken over by the Resolution Professional (RP), and key decisions are made by the Committee of Creditors (CoC).

Role of Resolution Professional

The RP acts as an interim manager responsible for:

- Managing operations
- Preserving asset value
- Conducting the resolution process

Role of the Committee of Creditors

The CoC, primarily composed of financial creditors, holds decision-making power. It approves resolution plans based on commercial wisdom.

This shift raises concerns:

- Reduced role of shareholders
- Limited participation of operational creditors
- Potential lack of transparency

Corporate Governance Challenges under Stress

Information Asymmetry

During insolvency, access to accurate financial information is often limited. Creditors may not have complete data, leading to inefficient decision-making.

Delay in Resolution

Although the IBC mandates strict timelines, delays are common due to litigation and procedural bottlenecks⁸.

Dominance of Financial Creditors

The CoC prioritizes financial creditors, often sidelining operational creditors and employees.

Ethical Concerns and Misuse

Instances of:

- Fraudulent transactions
- Asset stripping
- Strategic insolvency filings

highlight governance failures both pre- and post-insolvency.

Lack of Accountability

Resolution Professionals and CoC decisions are often shielded under “commercial wisdom,” limiting judicial scrutiny⁹.

Role of Adjudicatory and Regulatory Authorities

National Company Law Tribunal (NCLT)

The NCLT acts as the adjudicating authority under IBC. It ensures procedural compliance but does not interfere in commercial decisions.

⁷ OECD, *Principles of Corporate Governance*, OECD Publishing (2015).

⁸ Ministry of Corporate Affairs, *Report on Insolvency Resolution Timelines in India* (2022).

⁹ Committee of Creditors of Essar Steel India Ltd. v. Satish Kumar Gupta.

Insolvency and Bankruptcy Board of India (IBBI)

The IBBI regulates insolvency professionals and agencies, ensuring ethical conduct and compliance.

Judiciary's Approach

Courts have emphasized limited intervention in CoC decisions, as seen in landmark rulings.

Judicial Trends and Case Analysis

Indian courts have played a crucial role in shaping insolvency jurisprudence.

- In *K. Sashidhar v. Indian Overseas Bank*, the Supreme Court upheld the supremacy of CoC's commercial wisdom¹⁰.
- In *Swiss Ribbons Pvt. Ltd. v. Union of India*, the constitutional validity of IBC was upheld, recognizing its importance in economic reform¹¹.

These cases highlight a governance model where creditor interests dominate, raising concerns about equitable treatment.

Pre-Insolvency Governance Failures

Corporate insolvency is often a result of governance failures such as:

- Lack of board independence
- Poor risk management
- Financial misreporting
- Weak internal controls

Examples of major corporate failures in India demonstrate how governance lapses lead to insolvency.

Need for Governance Reforms

To strengthen corporate governance during insolvency, the following reforms are suggested:

Enhanced Transparency

- Mandatory disclosure norms
- Digital information systems

Balanced Stakeholder Representation

- Inclusion of operational creditors in decision-making

Strengthening Accountability

- Clear liability for insolvency professionals
- Oversight of CoC decisions

Capacity Building

- Strengthening NCLT infrastructure
- Training insolvency professionals

Preventive Governance Mechanisms

- Early warning systems
- Improved audit frameworks

2. Conclusion

Corporate governance under insolvency conditions is a complex and evolving area in India. The Insolvency and Bankruptcy Code, 2016 has significantly improved the

insolvency resolution landscape by introducing a structured and time-bound process. However, the stress of insolvency exposes inherent weaknesses in governance mechanisms. While the shift to a creditor-driven model has enhanced efficiency and recovery rates, it has also raised concerns regarding transparency, accountability, and equitable stakeholder treatment. Governance challenges such as information asymmetry, delays, and ethical issues continue to persist. A balanced approach that integrates strong governance principles into insolvency proceedings is essential for ensuring fairness and sustainability. Strengthening institutional capacity, enhancing transparency, and promoting accountability will help create a resilient insolvency framework capable of addressing future financial crises effectively.

¹⁰ K. Sashidhar v. Indian Overseas Bank.

¹¹ Swiss Ribbons Pvt. Ltd. v. Union of India.